

Message Text

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USEEC ALSO FOR EMBASSY
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DEPARTMENT PASS FEDERAL RESERVE BOARD; TREASURY FOR
DONALD E. SYVRUD

E.O. 11652: GDS
TAGS: EFIN, EGEN, PINT, UK
SUBJECT: RUN-UP TO THE BUDGET
SUMMARY: THE ANNUAL PROCESS OF RESOURCE ALLOCATION WHICH
CULMINATES IN THE CHANCELLOR OF THE EXCHEQUER'S BUDGET
MESSAGE IS ABOUT CONFLICTING INTERESTS, NATIONAL PRIORI-
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TIES, AND THE ADJUSTMENT OF ECONOMIC POLICY VARIABLES.
THE CHANCELLOR IS SCHEDULED TO PRESENT A BUDGET LIKELY T
CONTAIN A NET STIMULUS OF ABOUT 2.5 BILLION POUNDS TO TH
HOUSE OF COMMONS ON APRIL 11. THIS YEAR'S BUDGET WILL B
ESPECIALLY INTERESTING BECAUSE IT IS PROBABLY THE LAST
FULL BUDGET BEFORE A GENERAL ELECTION. THE VARIOUS PAR-
TIES AND INTEREST GROUPS, PARTICULARLY THE LIBERALS, WIL

BE TRYING TO INFLUENCE THE FINAL SHAPE OF THE BUDGET AND THERE IS A HEIGHTENED INTERNATIONAL INTEREST IN THE MAGNITUDE AND SHAPE OF THE LIKELY BRITISH CONTRIBUTION TO WHATEVER PATTERN OF "CONCERTED ACTION" EMERGES AT THE JULY SUMMIT IN BONN. OUR CURRENT ASSESSMENT IS THAT THE BUDGET AS PROPOSED BY THE CHANCELLOR WILL EMERGE LARGELY INTACT. IF NOT, THE LIKELIHOOD OF AN EARLY GENERAL ELECTION WOULD BE INCREASED. END SUMMARY.

THE MACRO CONTEXT

1. THE BUDGET IS ONE OF THE PRINCIPAL MEANS BY WHICH THE GOVERNMENT INFLUENCES THE OVERALL LEVEL OF DEMAND IN THE ECONOMY. THE CURRENT MACROECONOMIC CONTEXT IS ONE OF SLACK DEMAND, EXCESS CAPACITY, SHARPLY LOWER RATES OF PRICE INCREASE, INCIPIENT CURRENT ACCOUNT SURPLUS, AND DIMINISHING PUBLIC SECTOR BORROWING. THESE FACTORS HAVE LED TO A GENERAL CONSENSUS THAT SOME FISCAL STIMULUS IS APPROPRIATE.

2. BRITAIN, HOWEVER, HAS COMMITTED ITSELF TO THE IMF TO HOLD THE PUBLIC SECTOR BORROWING REQUIREMENT (PSBR) TO 8.6 BILLION POUNDS IN FY 78/79. ON UNCHANGED POLICIES, THE OUTLOOK WOULD BE FOR A PSBR OF 6 TO 6.5 BILLION POUNDS. IT IS THIS FORECAST THAT GENERATED A CONSENSUS THAT A 2.0 TO 2.5 BILLION POUND NET INJECTION IS THE MOST THE CHANCELLOR CAN PRUDENTLY DO IN THE BUDGET. ANYTHING

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MORE, IT IS ARGUED, WOULD JEOPARDIZE CONTROL OF THE GROWTH IN THE MONETARY AGGREGATES WHILE PROVOKING A TORRENT OF IMPORTS, FURTHER ERODING IF NOT ELIMINATING BRITAIN'S ANTICIPATED CURRENT ACCOUNT SURPLUS. THIS BALANCE OF PAYMENTS CONSTRAINT LOOMS LARGE IN THE CHANCELLOR'S FIELD OF VISION. IT HAS INDUCED PUBLIC EXPRESSIONS OF CAUTION FROM BOTH THE CHANCELLOR AND THE PRIME MINISTER ABOUT LIMITS TO WHICH FISCAL POLICY CAN BE PUSHED WITHOUT JEOPARDIZING HARD-WON INTERNATIONAL CONFIDENCE IN THE STABILITY OF THE UK ECONOMY.

3. MONETARY POLICY WILL ALSO OCCUPY AN IMPORTANT PLACE IN THE CHANCELLOR'S MESSAGE. IN THIS CONTEXT IT IS LIKELY THAT SOME REFERENCE TO EXCHANGE RATE POLICY WILL BE MADE. WITH REGARD TO THE MONEY SUPPLY, IT IS WIDELY ANTICIPATED THAT HE WILL DEPART FROM THE CURRENT PRACTICE OF SETTING A SINGLE, ANNUAL M3 TARGET BY ANNOUNCING HIS INTENTION TO REVIEW THE INITIAL M3 GROWTH RATE EITHER SEMI-ANNUALLY OR QUARTERLY. THE NEW M3 TARGET MAY BE marginally BELOW THE CURRENT 9-13 PERCENT RANGE. A SLIGHTLY LOWER TARGET WILL UNDERLINE THE CHANCELLOR'S INTENTION TO KEEP THE AGGREGATES UNDER CONTROL, A DEMONSTR

TION OF MORE THAN PASSING SIGNIFICANCE TO A FINANCIAL
COMMUNITY, BOTH DOMESTIC AND INTERNATIONAL, WHICH IS
AWARE THAT THE CURRENT TARGET WILL BE EXCEEDED. IN FACT
M3 HAS GROWN AT AN ANNUALIZED RATE OF 18 PERCENT OVER
THE PAST 6 MONTHS CAUSING INFLUENTIAL MARKET ANALYSTS

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TO EXPRESS ALARM ABOUT THE IMPLICATIONS FOR INFLATION
AND THE BALANCE OF PAYMENTS.

4. THE GOVERNMENT PREFERS TAX CUTS TO INCREASED PUBLIC
SPENDING AS THE MAIN METHOD OF STIMULUS. IT HAS ALREADY
ANNOUNCED EXPENDITURE PLANS WHICH WILL ADD ABOUT 3 PER-
CENT TO THE VOLUME OF EXPENDITURE IN THE COMING FISCAL
YEAR AND IS UNWILLING TO GO MUCH BEYOND THOSE PLANS. AS
A RESULT, REQUESTS FROM VARIOUS SPENDING DEPARTMENTS FOR

ADDITIONAL RESOURCES FROM THE BUDGETARY CONTINGENCY RESERVE WHICH ALREADY AGGREGATE TO A FIGURE OF ABOUT 750
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MILLION POUNDS -- THE SIZE OF THE RESERVE ITSELF -- ARE BEING RESISTED BY THE CHANCELLOR. CURRENT INDICATIONS ARE THAT HE WILL PROCEED IN HOLDING SUCH COMMITMENTS TO UNDER HALF THAT FIGURE AND THOSE WILL BE MOSTLY IN THE AREA OF TRANSFER PAYMENTS.

THE INTEREST GROUPS AND THE BUDGET

5. HAVING SET OUT THE MAJOR BUDGET ISSUES, IT IS INSTRUCTIVE TO SURVEY PROPOSALS BEING ADVANCED BY THE PRINCIPAL INTEREST GROUPS: THE POLITICAL PARTIES, ORGANIZED LABOR AND THE BUSINESS COMMUNITY.

THE LABOR PARTY

6. THE BUDGETARY INITIATIVE LIES WITH THE PARTY IN POWER AS A PARTY COMMITTED TO A GROWING PUBLIC SECTOR, LABOR HAS HAD TO SWALLOW HARD SINCE THE MIDDLE OF 1975. IT PRESIDED OVER REDUCTION IN THE VOLUME OF PUBLIC EXPENDITURE AS WELL AS THE FIRST SUSTAINED POST-WAR DECLINE IN REAL INCOMES. THERE WAS OBVIOUS PAIN IN THE PARTY WHEN FIRST PLANNED AND THEN ACTUAL SPENDING WAS PARED. HOWEVER, THE LARGELY MODERATE CABINET SUPPORTED THE CHANCELLOR IN OVERRIDING THE OBJECTIONS OF ITS MORE LEFT-WING MEMBERS. THE VIEW PREVAILED THAT A STABILIZATION OF BRITAIN'S FINANCIAL POSITION WAS PARAMOUNT SINCE WITH NO IMPROVEMENT IN THAT AREA, THE FORCE OF ANY FISCAL STIMULUS WOULD BE QUICKLY DISSIPATED BY MORE RAPID INFLATION.

7. IN THE WAKE OF THE DECEMBER 1976 AGREEMENT WITH THE IMF, BRITAIN'S FINANCIAL POSITION, IN PARTICULAR ITS EXTERNAL FINANCIAL POSITION, IMPROVED BEYOND ALL EXPECTATIONS. YET, THE RATE OF REAL ECONOMIC GROWTH IN 1977
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REMAINED CLOSE TO NIL. AS IT BECAME CLEAR THAT THE ECONOMY HAD STABILIZED AND NORTH SEA OIL WAS INCREASING AVAILABLE RESOURCES, VARIOUS GROUPS WITHIN THE PARTY BEGAN PRESSING PUBLICLY FOR A SUBSTANTIAL STIMULUS TO THE ECONOMY IN THE APRIL BUDGET.

8. LABOR'S LEFT-WING ARGUED THAT THE CHANCELLOR SHOULD

INCREASE PUBLIC EXPENDITURE WELL BEYOND THE PLANNED LEVELS AS THE MAIN ELEMENT IN BOOSTING ECONOMIC GROWTH. IT URGED THAT ADDITIONAL RESOURCES BE CHANNELLED INTO PUBLIC SERVICES, PARTICULARLY HOUSING AND HEALTH, INTO INCREASING THE LEVEL OF PUBLIC OWNERSHIP IN THE ECONOMY, INTO HIGHER TRANSFER PAYMENTS AND INTO THE FINANCING OF REDUCED INCOME TAXATION AT THE LOWER END OF THE INCOME DISTRIBUTION. THE NET STIMULUS IT PROPOSED WAS ABOUT 4 BILLION POUNDS. IMPORT CONTROLS WERE ADVOCATED AS A MEANS OF PREVENTING A MAJOR DETERIORATION IN THE CURRENT ACCOUNT.

9. AT THE OTHER EXTREME OF THE PARTY, THE RIGHT-WING MANIFESTO GROUP URGED A MORE MODEST NET STIMULUS OF 2.5 BILLION POUNDS WITH THE EMPHASIS ON REDUCED DIRECT TAXATION. IT ACCEPTED PLANNED PUBLIC EXPENDITURE INCREASES AS SET OUT IN THE JANUARY 1978 WHITE PAPER. THE MANIFESTO GROUP EXPRESSED AN UNDERSTANDABLE FEAR ABOUT THE CURRENT ACCOUNT IMPACT OF ANY LARGER PROGRAM. IT IS STRONGLY OPPOSED TO THE KIND OF IMPORT CONTROLS ADVOCATED BY THE TRIBUNE GROUP.

THE CONSERVATIVE PARTY

10. PHILOSOPHICALLY, THE CURRENT TORY LEADERSHIP IS FIRMLY ROOTED IN CONSUMER SOVEREIGNTY AND THE ABILITY OF THE MARKETPLACE TO PRODUCE OPTIMUM SOLUTIONS TO ECONOMIC PROBLEMS. THIS PREDISPOSITION SHAPES CONSERVATIVE VIEWS WHICH, BROADLY SPEAKING, FAVOR A DECLINING SHARE FOR PUBLIC

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LIC EXPENDITURE IN TOTAL OUTPUT AND PROVIDING FEWER PUBLIC SERVICES MORE EFFICIENTLY. IN ADDITION TO REDUCING TAXES, THE TORIES ALSO FAVOR A SIGNIFICANT SHIFT AWAY

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FROM DIRECT AND TOWARD INDIRECT TAXATION. AS THE PRINCIPAL OPPOSITION, THE CONSERVATIVE PARTY MUST REACT TO BUDGET MEASURES. WITH THEIR EYES SET ON THE COMING ELECTION, THE TORIES WILL PREDICTABLY FIND FAULT WITH THE LIKELY TAX CUTS, ARGUING THAT MUCH LARGER CUTS WOULD BE NEEDED TO OFFSET FULLY THE FISCAL DRAG BUILT UP SINCE THEY LEFT OFFICE IN 1974.

THE LIBERAL PARTY

11. THE LIBERALS SEE THE BUDGET AS THE MAJOR TEST OF
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THEIR INFLUENCE ON THE GOVERNMENT. EACH PARTY IS APPROACHING THE BUDGET WITH VERY DIFFERENT GOALS. LABOR WANTS TO PRESENT A PACKAGE TAILORED TO WIN IT THE LION'S SHARE OF PUBLIC CREDIT, DESIGNED TO ENSURE PASSAGE WITHOUT DAMAGING AMENDMENTS, AND SKEWED TO GIVE DISPROPORTIONATE BENEFITS TO THOSE VOTERS ON WHOSE SUPPORT LABOR DEPENDS. IN SHORT, LABOR SEEKS A BUDGET WHICH WILL LEAVE NO DOUBT WHO IS IN THE DRIVER'S SEAT.

12. THE LIBERALS, AWARE OF THE LIMITS OF THEIR POSITION, WANT TO DEMONSTRATE THAT THEY CAN MOVE LABOR TOWARD ACCEPTING SOME VERSION OF THEIR PROGRAM FOR A MAJOR REDUCTION IN INCOME TAXATION. JUST HOW FAR THEY GO IN

INSISTING THAT THE CHANCELLOR AGREE TO THEIR IDEAS IS NOW BEING CAREFULLY WEIGHED BY THE LIBERAL HIGH COMMAND. IN PRIVATE TALKS WITH THE CHANCELLOR, AND IN AN APRIL 5 PRESS CONFERENCE, THEY PUT FORWARD PROPOSALS TO REDUCE DIRECT TAXATION BY 4.4 BILLION POUNDS, ABOUT TWICE WHAT THE CHANCELLOR IS PREPARED TO ACCEPT. THE CHANCELLOR HAS REPORTEDLY ARGUED THAT BY MOVING TOWARD LIBERAL POSITIONS ON PROFIT SHARING AND TAX REDUCTIONS FAVORABLE TO SMALL BUSINESSES, LABOR HAS MORE THAN DELIVERED ON ITS SIDE OF THE BARGAIN. THE LIBERALS ARE UNWILLING TO ACCEPT THIS AND CONTINUE TO BELIEVE THAT SOME GIVE ON INCOME TAXATION IS STILL POSSIBLE.

13. TO OFFSET SOME OF THE IMPACT OF THAT INCOME TAX CUT, THE LIBERALS SUGGEST INDIRECT TAX INCREASES OF ABOUT 2 BILLION POUNDS. THESE INCLUDE STANDARDIZING

VAT AT 10 PERCENT, HIGHER EXCISE TAXES, AND A 1.5 PERCENT SURCHARGE ON EMPLOYERS' PAYROLL TAXES. THESE INCREASES WOULD IMMEDIATELY RAISE RETAIL PRICES (BY AN

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ESTIMATED 1.5 PERCENTAGE POINTS WITH A FURTHER PERCENTAGE POINT BEING ADDED OVER THE ENSUING 12 MONTHS AS THE EFFECTS OF THE PAYROLL TAX ARE FELT), SOMETHING LABOR IS DEAD SET AGAINST GIVEN THE POSSIBILITY OF AN AUTUMN ELECTION AND THE NEED FOR A FAVORABLE ENVIRONMENT FOR THE EXTENSION OF INCOMES POLICY BEYOND THE END OF THE CURRENT PAY ROUND. WHILE THERE ARE INDICATIONS THAT LIBERAL MPS ARE PREPARED TO FIGHT HARD TO ENSURE THAT THEIR TAX PROPOSALS ARE INCLUDED IN THE FINANCE BILL, THERE ARE EQUALLY FIRM INDICATIONS THAT THE CHANCELLOR AND THE PRIME MINISTER WILL RESIST GOING MUCH BEYOND AGREEING TO THE LIBERALS' DEMAND FOR THE INTRODUCTION OF LEGISLATION TO ALLOW THE ESTABLISHMENT OF A PROFIT-SHARING SCHEME AND SOME MEASURES TO AID SMALL BUSINESS.

INDUSTRY

14. AFTER RECEIVING SATISFACTION ON MANY OF ITS BUDGET PROPOSALS IN 1977, THE CONFEDERATION OF BRITISH INDUSTRY MAY NOT ACHIEVE THE SAME DEGREE OF SUCCESS ON APRIL 11. CBI IS STRONGLY URGING THAT THE CHANCELLOR CUT INCOME TAXATION BY 2.5 BILLION POUNDS IN SUCH A WAY THAT MIDDLE- AND UPPER-INCOME GROUPS BENEFIT MOST. OTHER ELEMENTS OF THE CBI PACKAGE ARE MUCH THE SAME AS IN PREVIOUS YEARS WITH CONCERN CENTERING ON SUCH AREAS AS THE RETENTION OF TAX RELIEF ON ACCUMULATED INVENTORY PROFITS, THE LEVEL OF CORPORATE INCOME TAXA-

TION, AND TAXATION OF CAPITAL GAINS.

ORGANIZED LABOR

15. THE TRADES UNION CONGRESS (TUC) HAS URGED A
SUBSTANTIALLY LARGER NET STIMULUS (3.6 BILLION POUNDS)
THAN HAS THE CBI. REDUCTION OF PERSONAL INCOME TAXA-
TION IS CENTRAL TO THE TUC, BUT INCREASES IN PUBLIC
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EXPENDITURE ALSO FIGURE IMPORTANTLY IN THE PACKAGE. THE MAIN TAX CUT, COSTING 1.9 BILLION POUNDS, WOULD INTRODUCE A REDUCED RATE (25 PERCENT) BAND FOR THE FIRST 1,000 POUNDS OF TAXABLE INCOME. THIS IS CLEARLY AIMED AT THOSE TAXPAYERS WHOSE INCOMES ARE NEAR THE NATIONAL AVERAGE AND WHO ARE MORE LIKELY TO BE SUPPORTERS OF THE LABOR PARTY. OFFSETTING THIS TAX CUT, IN A MINOR WAY, IS A 200 MILLION POUND REDUCTION IN EXPENDITURE-BASED TAX ALLOWANCES. THE TUC URGES PUBLIC EXPENDITURE INCREASES OF A BIT LESS THAN A BILLION POUNDS SPREAD
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AMONG EMPLOYMENT AND TRAINING MEASURES, EDUCATION, SCHOOL MEALS, CONSTRUCTION, AND THE HEALTH SERVICE. THE REMAINING BILLION POUNDS WOULD GO TO INCREASED TRANSFER PAYMENTS (PENSIONS, CHILD BENEFITS, ETC.).

TACTICS

16. THE LIBERALS' PACT WITH THE GOVERNMENT, THE IMPORTANCE OF THE MINOR PARTIES, AND THE PROXIMITY OF AN ELECTION MAKE THE TACTICS OF ENACTING THE BUDGET

MORE IMPORTANT IN THE SHORT TERM THAN THE PROPOSALS THEMSELVES. AFTER THE CHANCELLOR DELIVERS HIS MESSAGE, THERE FOLLOWS A WEEK OF GENERAL DEBATE. THIS IS CAPPED BY A VOTE ON THE BUDGET RESOLUTION AUTHORIZING GOVERNMENT DEPARTMENTS TO CONTINUE SPENDING PUBLIC FUNDS FOR 90 DAYS, PENDING THE ENACTMENT OF THE FINANCE BILL IMPLEMENTING THE BUDGET PROPOSALS. NO DIFFICULTY IS EXPECTED IN WINNING A MAJORITY FOR THE BUDGET RESOLUTION. THE FINANCE BILL IS THEN INTRODUCED AND GIVEN ITS SECOND READING. THE VOTE ON THE SECOND READING GIVES THE LIBERALS THEIR FIRST OPPORTUNITY TO BREAK WITH THE GOVERNMENT. THEN FOLLOWS THE COMMITTEE STAGE WHEN AMENDMENTS TO THE GOVERNMENT'S PROPOSALS CAN BE OFFERED. IT IS IN THIS PERIOD THAT GOVERNMENT COULD BE SADDLED WITH A SERIES OF DEFEATS ON MANY OF ITS PROPOSALS. FINALLY, THE BILL IS RETURNED TO THE FLOOR OF THE COMMONS WHERE THE GOVERNMENT CAN ATTEMPT TO REVERSE SOME OR ALL OF THE AMENDMENTS.

17. AT PRESENT, THE LIBERALS APPEAR TO BE GETTING

PRECIOUS LITTLE SATISFACTION FROM THE GOVERNMENT ON
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THE KEY ISSUE OF THE MAGNITUDE OF THE INCOME/TAX REDUCTIONS. THIS IS UNLIKELY TO CHANGE BEFORE APRIL 11. THUS THE LIBERALS WILL HAVE TO DECIDE JUST HOW HARD THEY WILL PUSH THE GOVERNMENT AFTER THE BUDGET RESOLUTION IS ADOPTED.

18. THE LIBERALS ARE AWARE OF THEIR CONTINUING LOW STANDING IN THE EYES OF THE ELECTORATE, AND MANY OF THEIR ACTIVISTS--IF NOT THEIR LEADERSHIP--WOULD LIKE TO END THE PACT SOONER RATHER THAN LATER. THEY ALSO ARE AWARE THAT THE GOVERNMENT WOULD DEARLY LIKE TO RETAIN THE OPTION OF REMAINING IN OFFICE (AND RENEWING THE PACT) BEYOND THIS FALL. THE LIBERALS WILL WANT TO PRESS THE GOVERNMENT TO ACCEPT SOME AMENDMENTS TO THE FINANCE BILL; AND, FOR ITS PART, THE GOVERNMENT NORMALLY LEAVES ITSELF SOME SCOPE FOR MINOR CONCESSIONS DURING THE COMMITTEE STAGE. ACCORDINGLY, THE LIBERALS ARE EXPECTED TO SUPPORT THE FINANCE BILL ON ITS SECOND READING, CONCENTRATING THEIR EFFORTS ON AMENDMENTS IN

COMMITTEE. HOW FAR THEY WILL BE ABLE AND WILLING TO GO IN PRESSING FOR AMENDMENTS THAT ARE CLEARLY ANATHEMA TO THE GOVERNMENT IS A KEY QUESTION.

19. TACTICAL CONSIDERATIONS ARE ALSO IMPORTANT TO THE TORIES. THEY MAY WELL INTRODUCE AMENDMENTS OF THEIR OWN TO ADD TO THE SIZE AND TO CHANGE THE EMPHASIS OF THE CHANCELLOR'S INCOME TAX REDUCTIONS. SUCH ACTION, THEY BELIEVE, WOULD ALLOW THEM TO GAIN FAVOR WITH THE ELECTORATE IN THE EXPECTED FALL ELECTION.

20. IT SEEMS CLEAR FROM THIS BRIEF SKETCH THAT THE BROAD ARENA FOR TACTICAL MANEUVER OPENS AN EVEN WIDER OPPORTUNITY FOR COSTLY MISCALCULATION. THE GAME IS ONE OF BLUFF, COUNTER-BLUFF AND SHIFTING PARLIAMENTARY ALLIANCES.

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UNVEIL A BUDGET THAT WILL CONTAIN SOME CONCESSIONS TO
THE LIBERALS BUT NONE LARGE ENOUGH TO DISTRACT ATTEN-
TION FROM WHAT WILL BE A DOCUMENT RESPONDING MOST
GENEROUSLY TO LABOR'S PRINCIPAL ELECTORAL SUPPORTERS
BUT NOT GIVING ENOUGH AWAY TO SERIOUSLY UNDERMINE
BRITAIN'S CURRENT ACCOUNT. WHILE WE DO NOT WISH TO
TRY TO PREDICT THE FORM IN WHICH THE FINANCE BILL
WILL EMERGE FROM ITS FINAL READING IN THE COMMONS, WE
ARE INCLINED TO BELIEVE THAT THE GOVERNMENT'S BUDGET
STRATEGY WILL NOT BE SERIOUSLY COMPROMISED. BUT
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SHOULD THAT NOT PROVE TO BE THE CASE, THE ODDS ARE
THAT CALLAGHAN WILL DECIDE TO CALL A SUMMER
GENERAL ELECTION RATHER THAN TRY TO HOLD ON UNTIL
THE FALL OR NEXT SPRING.

22. WHATEVER ITS DOMESTIC IMPLICATIONS, THE COMING BUDGET WILL CONTAIN THE OUTLINES OF BRITAIN'S CONTRIBUTION TO DEALING WITH THE FIVE MAJOR GLOBAL ECONOMIC PROBLEM AREAS SET OUT IN THE PRIME MINISTER'S RECENT FINANCE HOUSES ADDRESS. (LONDON 4278 - NOTAL)
A REAL GROWTH RATE OF ABOUT 3 PERCENT, PROBABLE IN THE WAKE OF THE BUDGET, WILL BE THE LARGEST ELEMENT IN THAT CONTRIBUTION.

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